

BEFORE THE MINNESOTA PUBLIC UTILITIES COMMISSION

Barbara Beerhalter	Chair
Cynthia A. Kitlinski	Commissioner
Norma McKanna	Commissioner
Robert J. O'Keefe	Commissioner
Darrel L. Peterson	Commissioner

In the Matter of a Request for Price Flexibility  
for CaroLine Services Offered by  
Northwestern Bell Telephone Company and  
Various Miscellaneous Tariff Changes  
Regarding CaroLine Services

ISSUE DATE: June 22, 1988

DOCKET NO. P-421/M-85-903

ORDER APPROVING MISCELLANEOUS  
TARIFF CHANGES AND DETARIFFING  
S E R V I C E , S U B J E C T T O  
DEMONSTRATION THAT DETARIFFED  
PRICES COVER EMBEDDED COSTS

PROCEDURAL HISTORY

On December 20, 1985 Northwestern Bell Telephone Company (Northwestern Bell or the Company) filed a request that the Commission detariff its CaroLine service, and that it approve minor modifications to that service offering.

The Department of Public Service (the Department or the DPS) investigated the matter and brought it before the Commission on May 24, 1988. James A. Gallagher appeared on behalf of the Company. Dennis Ahlers, Special Assistant Attorney General, appeared on behalf of the Department. Michael Bradley, Assistant Attorney General, appeared on behalf of the Office of the Attorney General.

The Department and the Office of the Attorney General did not oppose the minor modifications the Company proposed to make to its CaroLine offering. They did oppose detariffing, however, on grounds that the regulatory reform legislation enacted in 1987 was now the sole means for granting pricing flexibility to telephone companies. Minn. Stat. Sections 237.57 through 237.62. Since Northwestern Bell did not follow the procedures necessary to request flexibility under that statute, the parties argued that none was available. Alternatively, they argued that flexibility should not be granted because the Company had given no assurance that detariffed prices would cover the Company's embedded costs.

Having heard the arguments of counsel, and having examined the entire record herein, the Commission makes the following findings and conclusions.

### FINDINGS AND CONCLUSIONS

The Commission finds that NWB's request that CaroLine services be tariffed is similar to a request NWB made several years ago that NWB's CENTRON services be deregulated (see the Commission's Findings of Fact, Conclusions of Law and Order issued September 11, 1984 and Order Denying Reconsideration and Amending Order issued December 31, 1984 in Docket Nos. P-421/M-83-466, P-421/M-84-24, 25, & 26.). Both CaroLine and CENTRON provide services similar to that available through PBX systems which are offered through private vendors.

In the CENTRON proceeding, the Commission detariffed CENTRON services, and required that NWB maintain the revenue requirement, expenses and investment associated with CENTRON in the regulated rate base and books of account. The Commission allowed NWB to negotiate CENTRON contracts freely, but required NWB to price CENTRON to recover at least cost, setting contribution according to market demand. NWB was also required to file price lists for the CENTRON components in lieu of a CENTRON tariff. Finally, NWB was required to file copies of each CENTRON contract at least one day prior to the effective date of the contract.

Because the Commission required CENTRON rates to be priced at cost or above and kept all revenues in the regulated base, NWB's local ratepayer, rather than NWB shareholders, would obtain the benefit of any contribution generated from CENTRON services. This would also ensure that the local ratepayer would not subsidize CENTRON at rates below cost.

Since the CENTRON decision was issued, the Minnesota State Legislature enacted Minn. Stat. Sections 237.57 through 237.65 which establishes an alternative form of rate regulation which is only applicable if a company elects to the alternative form under Minn. Stat. Section 237.58, subd. 1.

A section of the new law, Minn. Stat. Section 237.59, classifies services such as CENTRON and CaroLine subject to emerging competition, if a company elects to be subject to regulation under the new law. A service subject to emerging competition is defined by the new law as a competitive service and is treated for regulatory purposes not unlike the Commission's treatment of CENTRON. Under Minn. Stat. Section 237.60, subd. 2, tariffs do not have to be filed for services subject to emerging competition. Instead, the company files price lists and can make increases in rates effective 30 days after notice. In addition, proposals to increase rates for services subject to emerging competition must be supported by an incremental cost study, or other cost study deemed acceptable by the Commission.

In addition to the specific regulatory treatment of emerging competitive services provided for in

Minn. Stat. Section 237.60, subd. 2, the new law also requires companies which elect to be subject to the new law to provide an embedded cost allocation between competitive and non-competitive services when a company initiates a proceeding to change the rates for non-competitive services (see, Minn. Stat. Section 237.62). This means that a company has to identify its embedded costs for competitive services and allocate a reasonable portion of the joint and common costs attributable to the competitive services to the competitive services.

The provisions of Minn. Stat. Section 237.62 were written into the law to ensure that all services of a regulated company, both competitive and non-competitive offerings shouldered their reasonable share of the company's embedded and joint costs. This protects the local ratepayer from subsidizing a regulated company's competitive services.

The new law's classifications, regulatory requirements and protections, however, only become effective when a company elects to regulation under the Minn. Stat. Section 237.58, subd.1. The Commission finds that NWB has not elected under the law such that CaroLine would be classified as subject to emerging competition. NWB's non-election places the Commission in the difficult position of interpreting how to treat a proposal for detariffing from a non-electing company given the law's provisions on competition, price flexibility or detariffing in telecommunications services.

The Commission finds it can either reject NWB's proposal or it can approve NWB's proposal with modifications designed to protect the company's local ratepayer from cross-subsidization of competitive services. The Commission finds that the first option, to reject NWB's proposal, is not consistent with the Commission's policy to allow more flexible regulatory treatment of services where, as in the case of CaroLine, alternative service providers exist (for the most recent example, see Order After Reconsideration, issued January 11, 1988, In the Matter of a Summary Investigation Into IntraLATA Toll Access Compensation for Local Exchange Carriers Providing Telephone Service Within the State of Minnesota, Docket No. P-999/CI-85-582, at pages 9-12).

The Commission finds that the second option, to approve NWB's proposal with modifications, is reasonable as long as the modifications meet the spirit, if not the letter of the regulatory flexibility as well as the regulatory protections written into Minn. Stat. Sections 237.57 - 237.65. Thus, the Commission will allow NWB to detariff CaroLine, but require that the following conditions be met:

- (1) In lieu of tariffs, price lists for NWB's CaroLine services must be filed which are supported by incremental cost studies. Rate changes for CaroLine service shall be made effective on 30 days notice and must be supported by incremental cost studies; and,
- (2) NWB must demonstrate that its CaroLine services are priced to cover their embedded costs and a reasonable portion of NWB's joint and common costs attributable to the CaroLine services.

#### ORDER

1. Northwestern Bell Telephone Company's CaroLine services are hereby detariffed.
2. Within 30 days of the service date of this Order NWB shall file with the Commission for its review and approval and serve upon the Department of Public Service and the Attorney General's Office, Residential Utilities Division, price lists for its CaroLine services which are supported by incremental cost studies. The prices contained in the list can be changed effective on 30 days notice and must be supported by an incremental cost study.
3. Within 30 days of the service date of this Order, NWB shall file with the Commission and serve upon the Department and the Attorney General's Office, documentation which shows that NWB's CaroLine services are priced to recover their embedded cost and a reasonable portion of NWB's joint and common costs attributable to the CaroLine services.

4. This Order shall become effective immediately.

BY ORDER OF THE COMMISSION

Mary Ellen Hennen  
Executive Secretary

(S E A L)